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IN THE

Supreme Court of the United States

OCTOBER TERM—1952

No. 185

SETH M. MILLIKEN,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF

JOHN W. BURKE, JR.,
Attorney for Petitioner.

JUDICIAL PRINTING CO., INC., 82 Beekman St., N. Y.—BEekman 3-9084-5-6

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COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

To the Honorable, the Chief Justice and Associate Justices of the Supreme Court of the United States:

Your petitioner, Seth M. Milliken, hereby respectfully requests this Honorable Court to issue a writ of certiorari to the United States Court of Appeals for the Second Circuit to review the decision and judgment of that court which modified the decision of the United States Tax Court in this proceeding (R. 28).

The Tax Court modified a determination by the Commissioner of Internal Revenue of a deficiency in petitioner's 1943 income tax, and determined an overpayment of said income tax liability (R. 13).

Opinions Below

The opinion of the Court of Appeals is reported at 196 F. 2d 135 and appears at pages 20 to 27 of the Record. The findings of fact and opinion of the Tax Court are reported at 15 T. C. 243 and appear at pages 5 to 12 of the Record.

Jurisdiction

The decision of the Court of Appeals was entered on April 10, 1952 (R. 28). A petition for rehearing was duly filed on April 25, 1952 (R. 29) and was denied without opinion on May 5, 1952 (R. 35).

This Court's jurisdiction to review the judgment below is based on Section 1254 of Title 28 of the United States Code.

Questions Presented

1. Was it not error for the Court of Appeals to hold that petitioner could only deduct as a capital loss, not an ordinary loss or expense, $33,411.29 he paid in 1942* in settlement of transferee liability asserted against him because in 1941 he had received assets of the dissolved Ellingwood Corporation in exchange for its corporate stock?

2. Was it not error for the Court of Appeals to hold petitioner should be taxed as short term, not long term, capital gain the $58,372.44 he received in 1942 (in three payments) for certain rights and assets he had previously obtained in exchange for corporate stock of Cotwool Manufacturing Corporation which he had owned for many years?

* The transactions herein occurred in 1942. However, the tax year involved is 1943 because of the change to "pay as you go".

With respect to two of these three payments, a subsidiary question is presented: When petitioner, having an option to buy certain stocks, notifies the optionor that he wishes to buy them, and therefore receives the difference between market value and option price, is this a "failure to exercise" the option within the meaning of the Internal Revenue Code, Section 117 (g) (2)?

Statutes Involved

Internal Revenue Code Sections 23(e), 111, and 117(a) (b) and (g) are involved. The relevant portions are set forth in Appendix A, below, pages 23 and 24.

Summary Statement of Facts

The Tax Court made certain findings of fact, incorporating by reference certain other facts stipulated by the parties. Other facts were established by allegations and admissions of the pleadings.

1. As to petitioner's payments as transferee of Ellingwood Corporation:

In December 1941, Ellingwood Corporation was dissolved and liquidated. Dr. Seth M. Milliken, the petitioner, owned 75% of its stock. In 1942 agents of the Bureau of Internal Revenue asserted deficiencies in the corporation's taxes, and asserted that Dr. Milliken was liable therefor as transferee. The claims were settled by payments slightly over 50% of the liabilities asserted and Dr. Milliken paid his pro rata share, $33,411.29. (Stipulation, R. 15, 16)

The Tax Court held that this was deductible as an ordinary loss. The Court of Appeals reversed and held that it was a capital loss.

2. As to petitioner's receipts with respect to his Cotwool Manufacturing Corporation stock:

In February 1922, Gerrish H. Milliken agreed that he would buy from the petitioner, Dr. Milliken, the latter's stock in Cotwool Manufacturing Corporation on petitioner's request, at book value. In March 1940, when the book value was about three times the market value, Dr. Milliken requested Gerrish to buy it. Instead, after negotiations, Gerrish and the petitioner entered into an agreement on June 28, 1940, as follows: Petitioner transferred his stock to Gerrish, Gerrish in exchange gave petitioner first, cash and notes for the market value (or about one-third the book value) and second, the right in petitioner to buy back his proportionate share of the underlying assets of the corporation at prices based on the same valuation, any time up to December 31, 1942. It will be noted that by thus using the same figure for sale price and repurchase option price, Dr. Milliken was in a sense automatically protected against undervaluation.

In 1942, the tax year in question, Dr. Milliken told Gerrish that he wanted to buy certain of the underlying assets (corporate stocks and securities of various textile mills) at the prices fixed in the 1940 agreement. Instead, the corporation paid him $25,458.13 in February and $2,390.11 in July, representing the difference between the then market price and the contract price for twelve of the securities covered by the 1940 agreement. (Tax Court's Findings, R. 6-8.) The Tax Court held that this was a short term capital gain and the Court of Appeals affirmed.

In November 1941 petitioner purchased another of the assets as he was entitled to do under the 1940 agreement, paying $3.05 for a $30,527.25 participation in a note of Whitney Manufacturing Corporation. This was the price fixed by the 1940 agreement, at 10 cents per thousand dol-

lars face amount. In March 1942 Dr. Milliken received $30,527.25 for the note (R. 7).

The Tax Court held that this $30,527.25 (less the $3.05 cost) was short term capital gain and the Court of Appeals affirmed.

Reasons for Granting the Writ

1. As to petitioner's payments as transferee of Ellingwood Corporation:

(a) The decision of the Court of Appeals herein is in direct conflict with the decision of the Court of Appeals for the Third Circuit on the same matter. It is also in conflict with several consistent decisions of the United States Tax Court and with decisions of certain United States District Courts. (See Point I-A of brief annexed.)

(b) The Court of Appeals herein has erroneously decided an important question of federal internal revenue laws which has not been, but should be, settled by this Court. (See Point I-B of brief annexed.)

2. As to petitioner's receipts with respect to his Cotwool Manufacturing Corporation stock:

(a) The Court of Appeals herein has erroneously decided an important and fundamental question of federal law, with respect to the administration of the federal income tax. The question of tax treatment of the second part of a "step transaction" constantly recurs in the administration of the federal income tax. Every time an exchange results in piecemeal gains other than cash installments, the same basic question is presented. This precise question has not been settled by this Court. At least two decisions of this Court on closely similar questions are probably in conflict with the decision of the Court of Appeals herein and are directly in conflict with the principles

relied on by the Court of Appeals in reaching its decision herein. The confusion created by the decision of the Court of Appeals herein should be removed by a decision of this Court.

(b) The decision of the Court of Appeals herein also necessarily involved an erroneous interpretation of Internal Revenue Code, Section 117 (g) (2), when that Court held that petitioner's notice to the optionor that he wished to buy the stocks subject to the option, followed by his receipt of the difference between the market value and the option price, was a "failure to exercise" the option. The common law rule both in the United States and in England is that such a notice exercises an option without more. The question is thus one of general importance in the tax law and is a question which has never been passed upon by this Court, but should be decided by it to clarify a novel but recurring point of tax law.

WHEREFORE your petitioner respectfully prays that a writ of certiorari be issued directed to the United States Court of Appeals for the Second Circuit in respect of its decision and judgment, modifying the determination of the United States Tax Court, for a review thereof by this Court, and for such other relief as to this Court may seem proper.

Dated: New York, New York, July 8, 1952.

SETH M. MILLIKEN,
Petitioner

By JOHN W. BURKE, JR.,
Attorney for Petitioner

Certificate of Counsel

I hereby certify that I have examined the foregoing petition for a writ of certiorari and in my opinion it is well founded and the cause is one in which the petition should be granted.

Dated: July 8, 1952.

JOHN W. BURKE, JR.,
Attorney for Petitioner